

Taxation of Credit Unions and Banks in Washington State

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Introduction

The following report provides a review of the tax status of credit unions and banks in Washington State and the nature of participation of credit unions in the PDPC-like entities of other states.

Tax Status of Credit Unions in Washington State

Credit unions are tax exempt because of their not-for-profit nature and cooperative structure. State-chartered credit unions are exempt from the business and occupation (B&O) tax for two reasons: 1) to recognize Washington State's credit unions' not-for-profit nature and cooperative structure, and 2) to create parity between federally-chartered and state-chartered credit unions. However, credit union service organizations (CUSOs) (depending on the type of business line included in the CUSO) may pay B&O tax as well as federal income tax.

Washington state-chartered credit unions pay state sales tax. Federally-chartered credit unions are specifically exempt from state sales tax under the Federal Credit Union Act, Section 1768, which states, “federal credit unions...shall be exempt from all taxation now and hereinafter imposed by the United States or by any State.” This is a costly issue when a state-chartered credit union buys a \$1 million building for their office or a branch and pays approximately \$80,000 sales tax while a similar transaction for a federally-chartered credit union does not result in any sales tax. The tax exemption has created a competitive disadvantage between federally- and state-chartered credit unions.

Federal Income Tax Status of Credit Unions

All state-chartered credit unions are exempt from federal income taxes under Section 501 (c) (14) of the Internal Revenue Code, but they must pay federal unrelated business income tax (UBIT) to the Internal Revenue Service. Federally-chartered credit unions are exempt from all

federal income taxes and most state taxes because they are considered an instrumentality of the federal government.

Tax Status of Banks Compared to Credit Unions in Washington State

Banks in Washington State pay tax, including the B&O tax and federal income tax, whereas credit unions do not. The following tables show a Washington State tax comparison for credit unions and banks.

Table 1: CREDIT UNIONS - Taxes Paid in Washington State

Description of Tax	Do WA <u>state-chartered</u> credit unions pay?	Do <u>federally-chartered</u> credit unions headquartered in Washington State pay?
Business & Occupational (B&O) Tax	No	No
Federal Income Tax	No	No
Payroll/Employment	Yes	Yes
Property Tax (real, real estate, and tangible)	Yes	Yes
Sales Tax	Yes	No
Use Tax	Yes	No

Table 2: BANKS - Taxes Paid by Banks in Washington State

Description of Tax	Do WA <u>state-chartered</u> banks pay?	Do <u>federally-chartered</u> banks pay?
Business & Occupational (B&O)	Yes, however mortgage-related assets are exempt from B&O	Yes, however mortgage-related assets are exempt from B&O
Federal Income Tax	Yes, unless the bank is a Subchapter S corporation	Yes, unless the bank is a Subchapter S corporation
Payroll/Employment	Yes	Yes
Property Tax (real, real estate, and tangible)	Yes	Yes
Sales Tax	Yes	Yes
Use Tax	Yes	Yes

Tax Status of Credit Unions in Other States

According to the 2008-2007 profile of the National Association of State Credit Union Supervisors (NASCUS), 47 states authorize state-chartered credit unions, while three states do not have a state credit union act and do not authorize state-chartered credit unions. Seventeen (17) states have state-chartered credit unions exempt from all state taxes. Of the 30 states that collect some type of state taxes from state-chartered credit unions, the most common type of state tax is sales and real property.

Tax Status of Financial Institutions in Oregon and California and the Nature of Their Participation in PDPC-like Entities

Oregon

Oregon Revised Statutes 723.752 addresses the application of tax statutes to credit unions. Under Oregon law and federal law, credit unions are exempt from income taxation. There is no such exemption for banks in Oregon statutes.

Oregon Revised Statutes 295 addresses the bank public funds pool. Some of the timelines and protections for these funds were amended by SB 832 this session. These changes were in response to Oregon banks' experiences with public funds and the closure of the Bank of Clark County, WA. Credit unions may only accept public funds up to the current allowable insured limit (\$250,000 per depositor through December 31, 2013). Credit unions introduced, but did not pass, SB 600 to allow a credit union pool for public funds.

California

In California, federally-chartered credit unions are exempt from federal income tax. Also, state-chartered credit unions are exempt from income tax. Furthermore, a credit union is classified as a nonprofit mutual benefit corporation under the California Tax Code. The income

tax exemption for state-chartered credit unions in California is cited in Section 23701y of the California Revenue and Taxation Code. In addition, credit unions pay property tax and sales tax. Banks are for profit and have the same tax status as corporations.

Under California Government Code 53637, credit unions and banks may act as depositories for public fund. They have the ability to receive agency deposits.

Conclusion

Washington State chartered credit unions and federally-chartered credit unions do not pay the B&O tax and the federal income tax. However, Washington State credit unions do pay state sales tax; whereas federally-charted credit unions do not. Banks on the other hand do pay the B&O tax and federal income tax in Washington State.

Under Oregon law, credit unions are exempt from income taxation. In addition, credit unions in Oregon may only accept public funds up to the current allowable insured limit (\$250,000 per depositor through December 31, 2013). In California, state- and federally-chartered credit unions are exempt from income tax, and credit unions may act as public depositories.